MODIFICATIONS, TERMINATIONS, AND CLAIMS

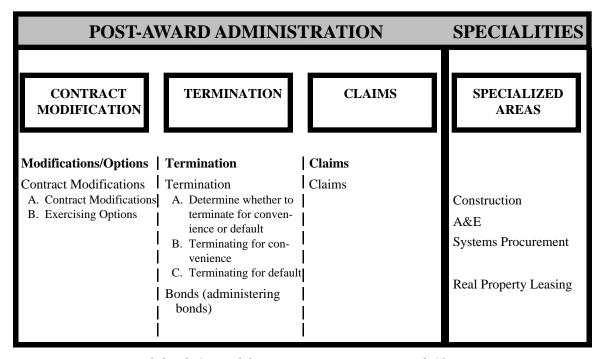


Exhibit 9-1. Modifications, Terminations, and Claims.

Learning Objectives

The learning objectives for this chapter are located at the front of the section or subsection to which they apply and are highlighted with gray shading. After completion of this chapter, you will be expected to know all the highlighted learning objectives for this chapter.

Exhibit 9-2. Learning Objectives.

CHAPTER INTRODUCTION

The post-award functions in this chapter involve changes in the rights and responsibilities of the parties as a consequence of contract modifications, terminations for convenience, or terminations for default. In addition, this chapter covers disputes over the terms and conditions of the contract.

9.1 CONTRACT MODIFICATION

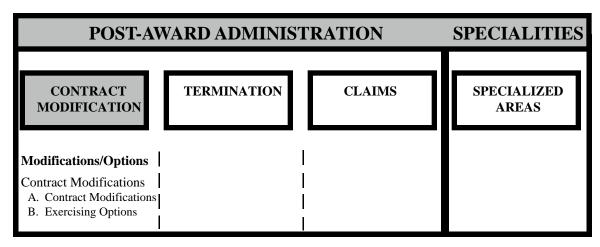


Exhibit 9-3. Contract Modification.

9.1.1 Modifications and Options

- Define contract modification.
- Distinguish unilateral from bilateral modifications.
- Explain "scope of work" as a constraint on the CO's ability to modify a contract.

FAR Part 43

• Describe the process for exercising options.

A contract modification is any written change in the terms of a contract. Modifications to contracts for non-commercial items generally can be either "unilateral" or "bilateral" On the other hand, FAR 52.212-4(c) allows only bilateral modifications of contracts for commercial items.

Unilateral Modifications

Unilateral modifications are issued and signed by the CO. Unilateral modifications are used for making:

- Administrative changes that do not affect the substance or price of the contract (e.g., changing the address of the payment office).
- Substantive changes that result in equitable adjustments in the contract price, delivery schedule, or both.

Most unilateral modifications are made under "Changes" clauses (i.e., FAR clauses 523.243-1, 243-2, or 243-3).

Equitable Adjustments

If a change order affects the contractor's costs or ability to meet the delivery schedule, the parties attempt to reach a bilateral agreement on an equitable adjustment in the contract's price and delivery terms. If an agreement cannot be reached, the CO unilaterally determines the amount. The contractor may then file a claim for the amount in dispute (see section 9.3).

Bilateral Modifications

Bilateral modifications (i.e., supplemental agreements) are negotiated and signed by both the CO and an agent of the contractor. A bilateral modification may be issued:

- To modify the terms of a contract that may not be unilaterally changed by the CO.
- In place of a unilateral modification when both parties negotiate and agree to the equitable adjustment prior to effecting the change.
- To incorporate an agreement on an equitable adjustment in price and other contract terms after issuance of a unilateral change.

Scope of Work

Generally, neither bilateral nor unilateral modifications may change the scope of work in a contract (although a bilateral change in scope may be proper when competition is not required for the additional work). Determining what changes are within the scope of the contract is a matter of judgement. The general rule is that scope of work circumscribes the intentions of the parties at the time of contract award. For example, a contract to fabricate and deliver office furniture cannot be modified to also provide for furnishing and installing microcomputers.

To Change or Not to Change

If the Livingston's wish to change the design of the house, they may negotiate a bilateral contract modification with the builder. The modification would incorporate the changes in specifications and also make any agreed upon corresponding changes in price or time for completion. While the Livingston's and the builder might verbally agree to some minor changes, any changes of substance should be in writing and signed by both parties.

Exercising an Option

FAR 17.2

Contracts often contain options for increasing the quantity being supplied to the Government. For example, a contract may provide for the delivery of 1,000 gargoyles at a specified price of \$8,000 per unit by March 30. The contract may also contain an option to supply an additional 500 units

at \$10,000 per unit by that same date, provided the option is exercised by January 1. If the Government needs the additional units, the CO can exercise the option unilaterally. However, before exercising the option, the CO must determine that:

- The additional quantity would meet an existing need.
- Funds are available to exercise the option.
- Exercising the option would be the best alternative for meeting the need, based either on a formal solicitation or on market research.

Note that service contracts also may include an option for extending the period of performance.

9.2 TERMINATION

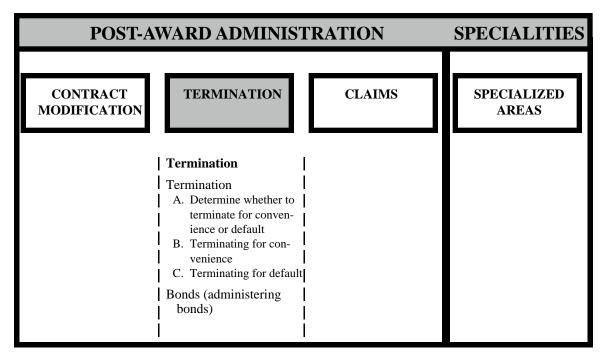


Exhibit 9-4. Termination.

A contract is entered into because the Government has a need to fulfill and the contractor agrees to fulfill it in return for specific compensation. The Government reserves the right to get out of a contract, in prescribed circumstances, by including termination clauses in its contracts (e.g., FAR clause 52.212-4 sections (l) and (m), which provide respectively for termination for convenience and for cause in contracts for commercial items).

9.2.1 Termination

• State circumstances that may signal the need for terminating a contract.

FAR Subpart 12.4 & Part 49

• Name the two major classes of termination actions.

In its contracts, the Government reserves the right to terminate (discontinue/halt) contract performance.

REASONS FOR TERMINATING CONTRACTS

- The Government's requirement has substantially changed or has been cancelled.
- The contractor fails, or is failing, to perform as required by the contract.

Exhibit 9-5. Reasons for Terminating Contracts.

Termination for Convenience

When the Government's requirement has changed substantially or been cancelled, the CO may exercise the Government's right to terminate the work as provided in the "Termination for Convenience of the Government" (T for C) clause. For example, suppose the contract is for one year of janitorial services. A few months after the contract starts, the agency relocates and the janitorial services are no longer required. The CO issues a unilateral notice terminating the remainder of the contract for the convenience of the Government. That action will usually be followed by a bilateral supplemental agreement reflecting the resulting change in price, disposition of property, etc.

Termination for Cause or Default

When the contractor is failing to perform, the CO may exercise the Government's right to terminate the work, in whole or in part, as provided in the "Default" clause (T for D) of contracts for non-commercial items or 52.212-4(m) in contracts for commercial items. For example, suppose a contractor is unable to secure the needed personnel and cannot perform the work of a fixed price contract. The CO may terminate the contract for default, secure services from another source, and bill the terminated contractor for the excess costs of reprocurement.

When the Government has sufficient evidence to suspect that delivery or other performance requirements are not likely to be met, the CO may choose to immediately take action rather than wait for the contract's delivery date. In these cases, the CO issues a "cure notice" if the time

MODIFICATIONS, TERMINATIONS, AND CLAIMS

remaining in the contract delivery schedule is sufficient to permit a "realistic" cure period of 10 days or more. If the cure notice fails to remedy the problem, then termination for default proceeds forthwith. If, on the other hand, the delivery date has arrived, the CO may issue a "show cause" letter or immediately initiate a default termination.

All contracts have a Termination for Convenience clause, but not all contracts have a Default clause. For example, cost-reimbursement R&D contracts with educational institutions do not have a Default clause.

Termination Issues

Terminations are often complicated, so much so that some agencies have even appointed Termination CO's to manage terminations and negotiate settlements on a full-time basis. Terminations are particularly complicated in production contracts when some work has been completed, some work is in progress, and materials have been purchased for work not started. For instance, some of the issues that might be discussed with the contractor when terminating include:

- Extent of the termination, the point at which the work stopped, and the Government's specific instructions for terminating the work.
- Terminating subcontracts.
- The termination inventory.
- Title transfer and delivery schedule for completed supplies and for manufacturing materials (e.g., partially completed supplies and materials, parts, tools, dies, jigs, etc.).
- Status of plans, drawings, and data that would have been delivered under the completed contract.
- Protection and preservation of any property in the Contractor's possession in which the Government has an interest.
- Preparation and submission of settlement proposals, including any related requirement for certified cost or pricing data.
- Any counterproposal by the contractor to continue work under the contract.

9.2.2 Bond Administration

• List five events in administering bonds.

FAR 49.402-3, 49.404, & 49.405

In section 7.1.1.5, you learned when to require the submission of bonds by a contractor. When administering contracts, the CO must ensure that the contractor maintains all bonds required by the contract and secures new bonds, when appropriate. Examples of situations that might call for special action on the part of the CO are shown in Exhibit 9-6.

SELECTED EVENTS IN ADMINISTERING BONDS		
Situation		CO's Action
Surety disqualified.	\triangleright	Ensure contractor obtains a new bond from another surety.
Surety requests information on the contractor's progress, payments, and/or estimated percentage of completion on the contract.	\triangleright	Furnish information.
Subcontractor or supplier, who has furnished or been requested to furnish labor and material, asks for name and address of surety given on payment bond.	>	Furnish information.
Option exercised.	\triangleright	Require a modified bond to reflect the change in the dollar amount, time period, or both.
Contract terminated for default.	>	Determine whether (1) the surety will arrange for performance or whether (2) the Government will reprocure at the surety's expense, to the extent the surety is liable for reprocurement costs.

Exhibit 9-6. Selected Events In Administering Bonds.

9.3 CLAIMS

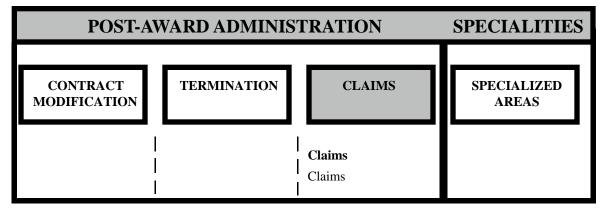


Exhibit 9-7. Claims.

- Define the term "claim."
- Describe the procedures for determining the validity of a claim made by a contractor.
- State how claims are handled; who decides; what are the rights of contractors when disputes arise.

FAR 33.2

Definition

A claim is a written demand or written assertion by a contractor (or the Government) that it is entitled to:

- Additional money "in a sum certain".
- Adjustment of contract terms (e.g., the delivery schedule) or a more favorable interpretation of the terms.
- Other relief arising under or related to the contract.

For example, suppose a CO unilaterally orders that widgets be painted with two coats of paint, instead of the one coat specified in the contract. The contractor would have to apply the extra coat. However, the contractor may request (i.e., claim) \$5,000 for the extra coat of paint over and above the original price of the contract. To constitute a claim, the contractor must submit the request for payment in writing to the CO. If the claim exceeds \$100,000, the contractor must also submit a certificate that:

- 1. The claim is made in good faith;
- 2. Supporting data are accurate and complete to the best of the contractor's knowledge and belief; and
- 3. The amount requested accurately reflects the contract adjustment for which the contractor believes the Government is liable.

CO's Response to the Claim

Upon receiving a claim, the CO may take the following steps:

- 1. Research the claim and prepare a finding of facts. Among other things, the CO may ascertain whether the claim is:
 - Timely?
 - Covered by an existing release of claims?
 - Barred by the contract clause at issue (e.g., clause at 52.219-10, which states that the determinations thereunder are not subject to the Disputes clause)?
 - Supported by sufficient, accurate, and complete data?
 - Factually correct?
 - Correct in its interpretation of the terms and conditions at issue and related case law?
- 2. Prepare the Government's initial position on the claim and on the amount of any equitable adjustment in price or other terms.
- 3. Discuss the claim with the contractor and try to reach a mutual agreement. For this purpose, COs are being encouraged to use any authorized, applicable Alternative Dispute Resolution procedure (such as mediation, arbitration, and minitrials, among others).
- 4. Prepare a decision on the claim, issue the decision in writing to the contractor, and initiate payment (if any).

In working through these steps, the CO generally draws on the advice and expertise of technical, audit, and legal office personnel.

In the case of the \$5,000 claim for the extra coat of paint, the CO may conclude that the contractor is entitled to an equitable adjustment in price but that the price should be increased by only \$3,800. If the two parties cannot negotiate a mutually agreeable settlement, the CO will render a final decision to only pay the contractor the lesser of the two amounts.

The Contractor's Appeal Rights

If the contractor disagrees with the CO's decision, the contractor may appeal the decision to the cognizant Board of Contract Appeals or to the courts.

9.4 SPECIALIZED AREAS

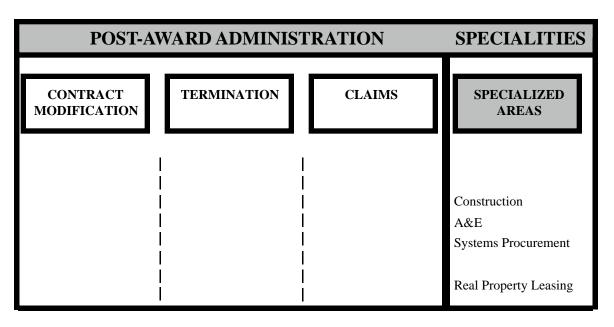


Exhibit 9-8. Specialized Areas.

There are categories of contracting (see Exhibit 9-9) that may require the use of procedures that supplement those discussed in the preceding chapters of this text.

SPECIAL CONTRACTING CATEGORIES

Construction FAR Part 36

Architect - Engineer (A&E)Services FAR Part 36

Major System Acquisition FAR Part 34 and OMB Circular A-109

Real Property Leasing Federal Property Management Regula-

tion (41 CFR 101-18)

Exhibit 9-9. Special Contracting Categories.

Each of these four categories requires special attention. Some of the categories are the subject of special courses. The six special categories of contracting are described in more detail below.

- **Construction.** Construction contracts typically include unique terms and conditions for such matters as:
 - Bonding.
 - Liquidated damages.
 - Permits.
 - Protection and clean-up of sites.
 - Utility services.
 - Progress payments based on percentage of completion.

Special and optional contracting forms are used, and special or alternate versions of clauses are numerous.

- Architect Engineer (A-E) Contracts. Special procedures apply to the selection of A-E sources for award. Moreover, A&E contracts are also distinguished by unique forms and clauses.
- Major System Acquisition. "Major System" means a combination of elements that function together to produce the capabilities required to fulfill a mission's need. The system may include hardware, equipment, and software. To be "major," a system

must meet the following catterns, TERMINATIONS, AND CLAIMS

- **DoD.** Total expenditures for research, development, test, and evaluation of the system are estimated to be more than \$75 million; or the total eventual expenditure, more than \$300 million (based on FY 80 constant dollars).
- **Civilian Agencies.** Total expenditures for the system are estimated to exceed \$750,000 (based on FY 80 constant dollars) or exceed the dollar level established by the agency pursuant to Office of Management and Budget (OMB) Circular A-109, "Major System Acquisitions."

In both DoD and civilian agencies, the Head of the Agency may designate any system a "major system." Major system acquisitions are subject to the special planning and control procedures in OMB Circular A-109.

• **Real Property Leasing.** The FAR does not prescribe guidelines for the leasing of real property. Instead, such guidance is provided in the Federal Property Management Regulation (FPMR), the General Services Acquisition Regulation (GSAR), and the specific statutes that authorize the leasing of real property.